

MISSOURI CIRCUIT COURT
TWENTY-SECOND JUDICIAL CIRCUIT
(ST. LOUIS CITY)

SCOTT B. LAKIN,
Director of the Department of Insurance for
the State of Missouri, in his capacity as the
Liquidator for General American Mutual
Holding Company;

And

ALBERT A. RIEDERER,
in his capacity as the Special Deputy
Liquidator for General American Mutual
Holding Company,

Plaintiffs,

vs.

MORGAN STANLEY & CO.
INCORPORATED,
a Delaware Corporation,
Serve at:
United States Corporation Company
2711 Centerville Road, Suite 400
Wilmington, Delaware 19808;

MORGAN STANLEY
A Delaware Corporation,
Serve at:
Corporation Trust Center
1209 Orange Street
Wilmington, Delaware 19801;

And

LEONARD RUBENSTEIN,
a Missouri Resident
Serve at:
105 Bon Chateau
St. Louis, Missouri 63141;

Defendants.

Cause No: 042-07300

Division No. 1

JURY TRIAL DEMANDED

PETITION

Scott B. Lakin, as Liquidator for General American Mutual Holding Company, and Albert A. Riederer, as Special Deputy Liquidator for General American Mutual Holding Company (“the Liquidators”), bring this action in their official capacity on behalf of General American Mutual Holding Company (“GAMHC”), GAMHC’s members and policyholders against Morgan Stanley & Co. Incorporated, Morgan Stanley, and Leonard Rubenstein (“Rubenstein”).

GAMHC, a mutual holding company, organized under the laws of the State of Missouri, was sole owner of GenAmerica (“GenAm”), which in turn owned General American Life Insurance Company (“GALIC”) (hereinafter collectively referred to as “General American”). As an insurer under Missouri’s Insurers Supervision, Rehabilitation and Liquidation Act, RSMo §§ 375.1150 to 375.1246 (the “Act”), General American is subject to regulation by the Missouri Department of Insurance (“MDI”). The Liquidators bring this action pursuant their authority granted under the Act.

I. PARTIES

A. PLAINTIFF

1. Plaintiff Scott B. Lakin is the Director of the Department of Insurance for the State of Missouri and the Liquidator of GAMHC duly appointed by a Missouri State Court pursuant to the laws of the State of Missouri regulating the business of insurance.

2. Plaintiff Albert A. Riederer is the Special Deputy Liquidator of GAMHC, duly appointed by the Director of the Department of Insurance for the State of Missouri. Riederer’s appointment was approved by the Liquidation Court pursuant to the laws of the State of Missouri regulating the business of insurance. § 375.1176.2.

3. Plaintiffs have standing to bring this action pursuant to Missouri's Insurers Supervision, Rehabilitation and Liquidation Act, RSMo §§ 375.1150 to 375.1246.

4. Plaintiffs bring this action pursuant to RSMo §§ 375.1182.1(12) and 375.1182.1(13), on behalf of General American Mutual Holding Company (hereinafter "GAMHC"), a Missouri Insurance Mutual Holding Company in statutory liquidation under the supervision of the Missouri State Courts pursuant to the laws of the State of Missouri regulating the business of insurance, and on behalf of GAMHC's members and policyholders.

B. DEFENDANTS

5. Defendant Morgan Stanley & Co. Incorporated is a corporation organized under the laws of the State of Delaware with its principal place of business in New York, New York. Morgan Stanley & Co. Incorporated does now, and at all times relevant to this Petition did, business within the State of Missouri.

6. Defendant Morgan Stanley & Co. Incorporated has as its registered agent for service in the State of Delaware the United States Corporation Company, 2711 Centerville Road, Suite 400, Wilmington, Delaware 19808.

7. Defendant Morgan Stanley ("MS") is a corporation organized under the laws of the State of Delaware with its principal place of business in New York, New York.

8. Defendant MS has, as its registered agent for service in the State of Delaware, the Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington, Delaware 198801.

9. At times relevant to this Petition, the entity now known as "Morgan Stanley" was known as Morgan Stanley Dean Witter & Co., and before that Morgan Stanley Dean Witter Discover & Co. At times relevant to this Petition prior to May 31, 1997, Morgan Stanley Group, Inc. was one of the predecessor entities to the entity now known as "Morgan Stanley" ("Morgan

Stanley Group, Inc.,” “Morgan Stanley Dean Witter Discovery & Co.,” and “Morgan Stanley Dean Witter & Co.” are hereinafter “MS Predecessors”). Because MS is the successor to the liabilities of each of the MS Predecessors, the allegations herein directed against MS refer not only to the current MS entity, but also to the time-relevant MS Predecessors, for whose actions and omissions MS is liable.

10. MS was and is the sole owner of Morgan Stanley & Co. Incorporated, as well as the ultimate parent of certain Morgan Stanley investment funds which, from 1993 through May, 1998, owned the vast majority of the stock of ARM Financial Group, Inc. MS at all times relevant to this Petition did, and continues to do, business within the State of Missouri.

11. As Defendant Morgan Stanley & Co. Incorporated was controlled by MS, as the investment funds that owned the vast majority of ARM Financial Group, Inc. stock were ultimately owned by MS, and as the acts of individual Morgan Stanley entity-employed persons, as complained of herein, were undertaken by employees of MS, Morgan Stanley & Co., Incorporated, and/or investment funds ultimately owned by MS and controlled by MS and/or Morgan Stanley & Co. Incorporated, and as both defendants acted in a collective and concerted manner in matters relevant to this Petition, including acting in a concerted manner to perpetuate a fraud on General American, and as MS and Morgan Stanley & Co. Incorporated aided and abetted in the acts of each other, Morgan Stanley & Co. Incorporated and MS are hereinafter collectively referred to as (“Morgan Stanley”).

12. During the relevant time, Morgan Stanley provided General American with investment banking services, including a variety of fiduciary advisory services. These services included a variety of financial analysis including the recommendation of the proposed demutualization of GAMHC, and related fiduciary advice and counseling to General American’s

Board of Directors.

13. Further, during time periods relevant to these claims, Morgan Stanley related entities owned ARM Financial Group, Inc. (previously known as Analytical Risk Management, hereinafter referred to as “ARM”), a company with whom General American had a “reinsurance agreement” relating to investment products.

14. Morgan Stanley also acted as investment banker to ARM while occupying the same role with General American.

15. Defendant Rubenstein was the President and Chief Executive Officer of Conning, a subsidiary of GAMHC. Rubenstein was also an Officer of General American. Rubenstein is now, and at all times relevant to this Petition was, a resident of the State of Missouri.

16. Defendant Rubenstein may be served at his home address of 105 Bon Chateau, St. Louis, Missouri 63141.

II. JURISDICTION & VENUE

17. The claims asserted herein are brought pursuant to the Insurers Supervision, Rehabilitation and Liquidation Act, RSMo §§ 375.1150 to 375.1246 (the “Act”).

18. At all times relevant to this Petition, General American’s principal office was located at 700 Market Street, within the City of St. Louis, Missouri.

19. This Court has jurisdiction over these actions.

20. Venue of all proceedings brought herein is proper in the City of St. Louis.

21. Missouri has adopted the Act for the purpose of regulating the business of insurance.

22. Missouri State Courts, pursuant to Missouri’s laws pertaining to the business of insurance, have taken jurisdiction over the liquidation of GAMHC prior to the filing of this lawsuit.

23. The McCarran-Ferguson Act provides that state law preempts federal law in cases involving state regulation of the insurance industry. 15 U.S.C. § 1012(b); *Munich American Reinsurance Co. v. Crawford*, 141 F.3d 585, 590 (5th Cir. 1998).

24. Under the McCarran-Ferguson Act, a federal statute is reverse-preempted by a state statute or law if: (1) the federal statute does not specifically relate to the business of insurance; (2) the state statute was enacted for the purpose of regulating the business of insurance; and (3) enforcing the federal statute would "invalidate, impair or supersede" the state statute. *United States Dep't. of Treasury v. Fabe*, 508 U.S. 491, 501 (1993); *Munich*, 141 F.3d at 595.

25. The McCarran-Ferguson Act "symbolize[s] the public interest in having the States continue to serve their traditional role as the preeminent regulators of insurance in our federal system and indicates the special status of insurance in the realm of state sovereignty." *Munich*, 141 F.3d at 595. This act reflects the strong federal policy of deferring the regulation of the insurance industry to the states.

26. Removal of this action to federal court would be improper because such removal would improperly interfere with the jurisdiction of Missouri State Courts over this matter as such jurisdiction is established by Missouri's laws regulating the business of insurance. *See, e.g., In re Amwest Sur. Ins. Co.*, 245 F.Supp 2d 1038, 1047 (D.Neb. 2002).

III. INTRODUCTION

27. In August 1999, General American sought protection from the Missouri Department of Insurance ("MDI"). This protection became necessary because of a severe liquidity crisis which threatened not only the existence of General American, but also the interests of hundreds of thousands of employees, policyholders and members, each of whom had a vested interest in General American's continued solvency.

28. The liquidity crisis followed a massive run on the assets of GAMHC's subsidiary, General American Life Insurance Company ("GALIC"), that occurred in early August, 1999. This "run on the bank" arose from "puts" exercised by the holders of some 6.5 billion dollars of General American Funding Agreements or Guaranteed Investment Contracts (hereinafter collectively "GICs"). Most of these GICs allowed their holders to require General American to repay 100% of principal and accrued interest on seven (7) days notice.

29. When the "run on the bank" occurred, General American became almost immediately liable to repay billions of dollars within a seven-day period. As General American could not possibly liquidate sufficient assets to meet the need for billions in cash on such short notice, General American was unable to repay the GIC holders. Accordingly, General American sought protection from the MDI.

30. Morgan Stanley was an integral part of the creation of the 7-day GICs and the idea to induce General American to sell the same, for the benefit of Morgan Stanley and to the fatal detriment of General American. Morgan Stanley, General American's own investment banker, misrepresented its skill, knowledge, intent and loyalty to General American, misrepresented facts regarding General American, failed to warn General American's Board of Directors of the impending disaster and failed to affirmatively communicate to General American's Board of Directors information and knowledge Morgan Stanley possessed regarding relevant matters in breach of Morgan Stanley's fiduciary duties to General American. Instead, Morgan Stanley put its own self-interest above the interests of its client, General American.

IV. GENERAL ALLEGATIONS

A. BACKGROUND OF MORGAN STANLEY

31. Morgan Stanley holds itself out as one of the world's largest diversified financial services companies, claiming a reputation for excellence in advice and execution on a global

scale. Morgan Stanley advises clients worldwide on strategic financial activities and services. Founded in 1935, Morgan Stanley markets to clients its asserted “excellence” in investment banking, claiming as its slogan “One client at a time.”

32. Morgan Stanley raises capital in the equity and debt markets and advises clients on mergers, acquisitions and restructurings. Morgan Stanley represents and warrants that it has unique expertise understanding, analyzing and dealing with rating agencies. Morgan Stanley made these representations and warranties to General American and General American relied upon them in engaging Morgan Stanley.

33. Morgan Stanley also represents and warrants that it is a worldwide leader in investment banking, mergers and acquisitions, underwriting of equity and equity-related transactions, high-yield debt financing, and corporate debt issuance. Morgan Stanley made these representations and warranties to General American and General American relied upon them in engaging Morgan Stanley.

34. Morgan Stanley conducts an extensive mergers and acquisitions business. Morgan Stanley represents to clients that it is able to structure and execute a wide range of complex domestic and international transactions including acquisitions, divestitures, mergers, joint ventures, corporate restructurings, shareholder relations, recapitalizations, spin-offs, exchange offers, leveraged buyouts and defenses against unsolicited takeover attempts. Morgan Stanley purports to analyze and develop the best business solutions for each individual client, and so represented all these skills, expertise and experience to General American. Morgan Stanley made these representations and warranties to General American and General American relied upon them in engaging Morgan Stanley.

35. Morgan Stanley also claims expertise relating to capital markets, trading and financial

research activities. Morgan Stanley represents that it provides analysis, structuring and distribution capabilities to institutional users of mortgage-backed securities. Further, Morgan Stanley solicits, structures and executes investment grade debt and related product businesses, including new public and private debt issues. Morgan Stanley also purports to establish and maintain an active dialogue with clients regarding the provision of advice on all such issues. Morgan Stanley made these representations and warranties to General American, and General American relied upon them in engaging Morgan Stanley.

36. Claiming to be involved in deal execution from start to finish, Morgan Stanley invites its clients to rely upon it to assess current and future market conditions. Morgan Stanley also undertakes the origination, structuring, marketing and pricing of public offerings and private placements of equity and equity-related securities. Morgan Stanley made these representations and warranties to General American, and General American relied upon them in engaging Morgan Stanley.

37. Morgan Stanley held itself out to General American, and to the business community, as one of the most, if not the most, comprehensive professional financial services companies in the world, with the ability to advise and assist its clients with any potential situation. Morgan Stanley claims expertise in all areas of financial analysis and services and by doing so, invites and induces clients to rely on its expertise when making important business decisions. Morgan Stanley made these representations and warranties to General American, and General American relied upon them in engaging Morgan Stanley.

38. General American hired Morgan Stanley as General American's Investment Banker in reliance on these representations of skill, knowledge, and loyalty as a fiduciary.

B. BACKGROUND OF ARM

39. Based in Louisville, Kentucky, ARM was founded in July 1993. From its inception

ARM specialized in the asset accumulation business, providing retail and institutional customers with products and services designed to serve long-term savings and retirement markets. ARM claimed that it specialized in integrated asset-liability management for the management of securities portfolio risk, touting its risk management procedures as permeating all facets of its business.

C. BACKGROUND OF MORGAN STANLEY'S RELATIONSHIP WITH ARM

40. Shortly after its inception in 1993, ARM received a substantial equity investment from investment funds owned, controlled and managed by Morgan Stanley, including, but not limited to, an investment fund owned by senior Morgan Stanley employees. In return for this investment, these Morgan Stanley funds eventually owned about 90% of ARM's equity.

41. Morgan Stanley made this investment of its own capital in ARM with the expectation that it could later liquidate its interest at a substantial profit.

42. Morgan Stanley controlled and dominated ARM. Morgan Stanley's ownership of ARM was so extensive that, pursuant to the rules of the National Association of Securities Dealers, ARM was deemed to be an affiliate of Morgan Stanley.

43. Moreover, ARM's Board of Directors was extensively populated with Morgan Stanley employees and other Morgan Stanley-controlled persons. ARM's Board of Directors included Morgan Stanley employee Colin Raymond even after Morgan Stanley divested its stake in ARM. In fact, a Morgan Stanley employee remained on ARM's Board of Directors on a continuous, uninterrupted basis up to and including the date that ARM collapsed and filed for Chapter 11 protection under the Bankruptcy Code of the United States.

44. At times relevant to this Petition, ARM's corporate by-laws included provisions prohibiting ARM's Board of Directors from taking any action without the presence of a Morgan Stanley-employed director.

45. Aside from its ownership interest in ARM, Morgan Stanley was the lead underwriter for both of ARM's public offerings and was also the lead underwriter for ARM's preferred offering. Through these offerings, Morgan Stanley and its investment funds made millions of dollars in profits from return on their investments and from investment banking fees.

46. Further, ARM retained Morgan Stanley as investment banker and financial advisor to deal with ARM's precarious financial condition.

47. Because of Morgan Stanley's dominance and control of ARM, the continuous presence of one or more Morgan Stanley employee on ARM's Board of Directors, and Morgan Stanley's sustained engagements as ARM's investment bankers, Morgan Stanley knew all of the facts relating to the acts, status, strategies, and intentions of ARM as alleged herein.

48. In an effort to build ARM's balance sheet, Morgan Stanley facilitated ARM's acquisition of Integrity Life Insurance Company and National Integrity Life Insurance Company (collectively the "Integrity Companies"). These acquisitions were an attempt to allow ARM to participate in the investment markets by providing a vehicle through which ARM could write its own GICs. However, while the acquisition of the Integrity Companies provided ARM with an initial entrée into the investment markets, the Integrity Companies did not possess adequate "ratings" to allow for the growth that Morgan Stanley needed if it was to realize large profits upon liquidating its investment in ARM.

D. BACKGROUND OF GENERAL AMERICAN

49. General American was a mutual life insurance company with a history dating back over 100 years. General American had focused on conservative, insurance related business. Focusing on this core business, General American grew to become the largest insurance company incorporated in Missouri.

50. General American was headquartered within the City of St. Louis, Missouri and

employed thousands of people. As a mutual insurance company, its owners were its policyholders/members.

E. GENERAL AMERICAN’S RELATIONSHIP WITH ARM

51. The relationship between ARM and General American initially consisted of a relatively minor marketing agreement, whereby ARM marketed General American GICs to “qualified plans,” generally pension plans. The General American GICs ARM marketed were relatively standard in the insurance industry. These GICs were not the extremely short put GICs that ARM later developed, and which were ultimately at the heart of General American’s liquidity crisis.

F. ARM DEVISES THE 7-DAY GIC

52. In 1994, ARM developed a new GIC product which ARM intended to market to the “non-qualified” market, which were primarily Money Market Funds regulated under SEC Regulation 2a-7. Because of the investment limitations imposed on these target customers by Federal Law, ARM designed a GIC with a “7-day put” feature, *i.e.* a contractual provision allowing the GIC purchaser to receive repayment of 100% of the invested principal, and any accrued interest, on 7-days notice, and without penalty. This short put feature contained no restriction on, or disincentive to, the customer’s right to “put” the GIC.

53. Because this new short put GIC was to be marketed to customers, including Money Market Funds, that either required, or highly desired, investment grade securities, Morgan Stanley and ARM realized that ARM could not attract significant business by selling these GICs as the product of ARM’s subsidiaries Integrity or National Integrity. Rather, ARM needed a “partner” insurance company with better credit ratings and a stronger balance sheet in order to make this new short put GIC a marketing success.

54. As early as 1994, ARM and Morgan Stanley knew of serious risks that would be

borne by the issuer of these short put GICs, including the risk of a ratings downgrade and the risk of a “run on the bank” scenario given the product’s extremely short put.

G. ARM BRINGS THE 7-DAY GIC TO GENERAL AMERICAN

55. Knowing ARM’s need for access to higher ratings, ARM, with the knowledge and acquiescence of, if not at the instigation of, Morgan Stanley, utilized its existing relationship with General American, and the business trust and goodwill created in that relationship, to convince General American to partner with ARM on ARM’s newly conceived short put GIC product.

56. ARM proposed that General American offer the new short put GIC as a General American product. As proposed by ARM, short put GIC investors would pay cash to General American in exchange for a General American short put GIC.

57. ARM, however, was not content to earn a percentage marketing fee on the new short put GIC product. Rather, both ARM and Morgan Stanley realized that if ARM could obtain access to the funds that the short put GIC investors paid General American, ARM, and Morgan Stanley as the majority owner of ARM, would benefit in two ways: first, ARM’s assets under management would grow, improving ARM’s balance sheet in the eyes of rating agencies and prospective buyers; and second, ARM could, by aggressively investing its share of the money from the GIC investors, earn higher profits than ARM could expect from a marketing fee.

58. Thus, ARM proposed a “reinsurance agreement.” The basic terms of the “reinsurance agreement” were that an ARM insurance company subsidiary (for a time National Integrity, then later Integrity) would receive one-half of the short put GIC deposits in exchange for that insurance subsidiary’s agreement to repay the deposits and applicable interest to General American if General American were required to repay the short put GIC investors.

59. ARM, with the knowledge and acquiescence of, if not at the instigation of, Morgan

Stanley, targeted General American and its higher rated balance sheet as ARM's partner to write and sell the short put GICs, for the benefit of ARM and Morgan Stanley, and to the detriment of General American.

60. Pursuant to ARM's request, certain General American management agreed to enter into a "reinsurance agreement" with ARM, through which ARM essentially "rented" General American's balance sheet so as to allow ARM to sell its investment products, predominantly short put GICs, under General American's higher credit rating.

61. Initiated in 1995, the "reinsurance agreement" continued substantially unchanged until late May 1999, when ARM, with the advice of Morgan Stanley, abandoned the relationship with General American. Just two months later, the liquidity crisis, caused by the mass puts of substantially all of the short put GIC product, caused the demise of General American.

H. THE SHORT PUT GICS' INHERENT FLAWS

(a) LIQUIDITY

62. Because of the extremely short put period for the short put GICs, and because of the lack of any penalty or disincentive to GIC purchasers exercising the put, it was essential that the assets backing these GICs be both highly liquid, and not subject to the risk of significant swings in market value. These assets, on the other hand, also had to provide a yield higher than the interest paid to GIC investors (this difference between the money paid to investors as interest, and the money earned by investing the GIC proceeds, is known as the "spread") in order for the short put GICs to be profitable for General American and ARM.

63. These requirements greatly reduced the potential universe of acceptable investments backing the short put GICs, and greatly increased the risk that the search for greater spreads between the interest owed to short put GIC investors and the yield of the assets backing the short put GICs would result in investments that were either unacceptably illiquid, unacceptably subject

to significant variation in market value, or both.

64. The inability to liquidate the assets which supported the short put GIC contracts was a major factor in General American's inability to meet the "run on the bank" which occurred in August 1999. Morgan Stanley recognized this potential problem with the short put GIC product as far back as 1994.

65. Morgan Stanley, as ARM's controlling owner and advisor at the time the short put GIC was devised, knew, or reasonably should have known, that the short put GIC presented unacceptable levels of risk, and further knew, or should have known that the short put GIC was, in essence, a "house of cards" that would inevitably collapse.

66. Morgan Stanley had a duty to advise General American's Board of Directors regarding this risk. Morgan Stanley failed to do so and instead misled General American's Board of Directors as to the existence, nature and extent of this risk.

(b) THE RATING AGENCY RISK

67. General American's short put GIC was a debt security rated by major credit rating agencies such as Moody's Investors Services.

68. The ratings assigned by these rating agencies to General American's GICs were crucial. Many of the purchasers of these short put GICs, including the Money Market Funds who were the primary target customer for these short put GICs, were either required (by statute or internal policy) or were highly desirous of, an "investment grade" rating. Moreover, should the rating subsequently fall below "investment grade," many of the target customers for the short put GICs would be compelled or expected to redeem their GICs.

69. This risk of ratings downgrade was known to ARM and Morgan Stanley in 1994, and was discussed between ARM and Morgan Stanley on multiple occasions between 1994 and the summer of 1999.

70. Moreover, both ARM and Morgan Stanley recognized that, because of the substantial financial interrelationship between General American and ARM, the rating agencies took the view that ARM and General American were so linked financially that a ratings downgrade for one of these entities would likely result in a ratings downgrade for the other.

71. Morgan Stanley had a duty to advise General American's Board of Directors regarding this risk. Morgan Stanley failed to do so and instead misled General American's Board as to the existence, nature and extent of this risk.

I. ARM'S INVESTMENT STRATEGY INCREASES THE RISK

72. ARM chose to invest its one-half of the short put GIC proceeds in a mix of assets which attempted to increase the spread at the expense of sufficient liquidity and market value stability. ARM's choice of investment assets backing the short put GIC included heavy concentrations of various classes of securities that did not guarantee anything near the level of liquidity or market value stability reasonably necessary to fund large redemptions by short put GIC holders.

73. ARM engaged in this investment strategy despite its knowledge, at all relevant times, that rating agency downgrades and a run on the bank were significant risks inherent in the short put GIC products.

74. Morgan Stanley likewise knew of these risks, knew the details of ARM's investment strategy, and knew of the risks inherent in ARM's strategy and actions. Moreover, Morgan Stanley knew that any one of many internal or external events could easily collapse ARM's "house of cards."

75. Morgan Stanley had a duty to advise General American's Board of Directors regarding the illiquidity of the assets backing the short put GICs. Morgan Stanley failed to do so and instead misled General American's Board of Directors as to the existence, nature, and extent

of this risk.

J. GENERAL AMERICAN'S BOARD OF DIRECTORS RETAINS MORGAN STANLEY

76. In October 1998, General American's Board of Directors retained Morgan Stanley as Investment Banker for General American. General American's Board of Directors relied upon Morgan Stanley's advice and expertise in connection with the Board's analysis of strategies to pursue in order to improve the value of General American to its policyholders/members.

77. By accepting this engagement, Morgan Stanley undertook fiduciary duties to General American beginning in October 1998, including duties of full candor, loyalty, and other duties attendant to a fiduciary relationship. Thereafter, Morgan Stanley owed a fiduciary duty and obligation to General American.

78. A substantial part of Morgan Stanley's representation of General American consisted of the evaluation of General American's financial status.

79. As General American had issued, through its relationship with ARM, billions of dollars in short put GICs, the analysis of the short put GIC product and its corresponding assets and liabilities was a significant and material aspect of Morgan Stanley's representation of General American.

K. ARM'S FINANCIAL CRISIS

80. While Morgan Stanley was representing General American, ARM's board of directors, including a Morgan Stanley employee, knew that ARM was suffering from severe financial troubles which necessitated an infusion of capital. ARM also recognized that its "Institutional Business," of which the General American short put GIC was the most significant part, was suffering from systemic problems, including risk of ratings downgrade, decline in market value, liquidity problems, and the fundamental problem posed by having extremely large

liabilities puttable on 7-days notice.

81. In December 1998, in an attempt to avert the crisis, ARM retained Morgan Stanley to assist it in raising capital with the hopes of avoiding ARM's collapse. Morgan Stanley accepted the engagement.

82. This engagement was contrary to the fiduciary obligations owed by Morgan Stanley to General American.

83. Through at least August, 1999, Morgan Stanley served as ARM's Investment Banker. During this time, Morgan Stanley was repeatedly, and specifically, advised of ARM's serious financial problems. Morgan Stanley owed General American a fiduciary duty of full and complete disclosure of those problems.

84. As far back as 1994, Morgan Stanley knew that the short put GIC product had the potential for enormous instability that could ultimately lead to a "run on the bank." As Morgan Stanley did not disclose this instability when it owned ARM, or while underwriting ARM's offerings, Morgan Stanley feared that ARM's collapse could cause Morgan Stanley to be the subject of substantial litigation and expose Morgan Stanley to the risk of substantial judgments.

85. Morgan Stanley had a duty to advise General American's Board of Directors regarding the existence, nature and extent of ARM's financial crisis, and the highly likely detrimental impact of the same on General American. Morgan Stanley failed to do so and instead misled General American's Board of Directors as to the existence, nature and extent of ARM's financial crisis and the highly likely detrimental impact of the same on General American.

L. MORGAN STANLEY'S MISCONDUCT

(a) MORGAN STANLEY'S FAILURE TO ADVISE GENERAL AMERICAN IN OCTOBER 1998

86. When Morgan Stanley was hired as General American's Investment Banker in October 1998, Morgan Stanley assumed fiduciary duties to its client, General American.

87. As part of the engagement, Morgan Stanley was provided unlimited access to General American documents and records so as to allow Morgan Stanley to properly advise as to whether GAMHC should undertake a proposed demutualization.

88. In undertaking the representation of General American, as its Investment Banker, Morgan Stanley agreed to conduct a thorough review of General American's financial condition and the condition of the market for the proposed demutualization.

89. Despite Morgan Stanley's knowledge regarding the inherent flaws in the short put GIC, and despite Morgan Stanley's knowledge of ARM's financial crisis, including but not limited to the knowledge Morgan Stanley gained as an owner of ARM, the knowledge Morgan Stanley gained through its repeated due diligence on ARM in connection with ARM's 1997 and 1998 sales of equity securities, and the knowledge Morgan Stanley gained through its continued presence on ARM's Board, Morgan Stanley failed to advise General American's Board of Directors of the short put GIC's problems or of ARM's precarious position and deepening financial crisis, and instead misled General American's Board of Directors as to the existence, nature and extent of these problems, all to General American's detriment.

(b) MORGAN STANLEY'S CONTRARY PRESENTATIONS IN EARLY 1999

90. In January 1999, Morgan Stanley made presentations to the respective Boards of ARM and General American. In these presentations, Morgan Stanley took starkly contradictory positions regarding the value and viability of the short put GIC programs, the prospects of ARM, and the existence and nature of the deepening crisis at ARM.

91. In a January 1999, presentation to ARM, Morgan Stanley, and its employee and officer Derek Kirkland, highlighted numerous risks faced by ARM, including:

- (a) An analysis of the short put GIC product that correctly concluded the short put GIC could prove disastrous to ARM.
- (b) Analysis of the numerous troublesome aspects of ARM's current holdings. Specifically, Morgan Stanley indicated that a ratings downgrade of ARM would be a substantial event risk, that ARM's absolute capital levels were problematic, that there was a significant exposure to short put GICs, that there was a significant exposure to large single GIC contracts, and that there was a risk of a General American downgrade.
- (c) That there was a strong likelihood, if not inevitability, that ARM would be downgraded by the ratings agencies.

92. To avoid these substantial problems, Morgan Stanley suggested that ARM reduce its GIC writings, develop an alternative partner to General American, and raise additional capital.

93. In a January 1999, presentation to General American's Board of Directors, Morgan Stanley and Derek Kirkland, although required to do so pursuant to their fiduciary duties, provided no warning to General American's Board of Directors regarding the fundamental problems of the short put GIC product and of ARM's crisis.

94. Instead, Morgan Stanley advised General American's Board of Directors that the GIC program was well-managed and that the GIC program should be part of General American's growth strategy. Rather than warn the General American Board of Directors about the deepening crisis at ARM and the risks associated with the GIC program, Morgan Stanley blithely counseled General American's Board of Directors to proceed forward with the demutualization Morgan Stanley recommended.

95. On February 18, 1999, Morgan Stanley made a second presentation to ARM's Board of Directors. This second presentation to ARM was almost identical to, and was equally as pessimistic as, Morgan Stanley's prior presentation to ARM.

96. In the presentation, Morgan Stanley again noted problems stemming from inadequate capital levels, from the large accumulation of short put GICs, from the exposure attendant on the

small number of GIC holders, and from the risk of a General American downgrade.

97. Further, Morgan Stanley specifically warned ARM about the declining book value of ARM's portfolio, ARM's need for capital, concerns relating to the composition of ARM's investment portfolio, and the possibility of a rating agency downgrade.

98. It was suggested that ARM terminate the General American relationship to avoid further exposure to short put GICs, and that a ratings agency downgrade would have "quite drastic" consequences.

99. Morgan Stanley knew that, if unreported to General American's Board of Directors, ARM's problems would likely imperil General American's financial well-being. However, Morgan Stanley failed to inform General American, its own client, of this vital information and instead misled General American's Board of Directors as to the existence, nature and extent of these problems.

(c) MORGAN STANLEY'S CONTINUED FAILURES TO DISCLOSE

100. On March 5, 1999, General American was downgraded by Moody's Investors Services. This downgrade brought General American within one downgrade step of a mandatory massive put by substantially all of the holders of short put GICs.

101. The precarious situation worsened throughout the spring and summer. All the while, Morgan Stanley refrained from advising General American's Board of Directors, its client, of the impending catastrophe. Morgan Stanley instead continued its misrepresentations to General American's Board of Directors regarding the existence, nature and extent of the problems.

102. While Morgan Stanley failed to warn General American's Board of Directors about the danger of its situation, the danger of the short put GIC, and of the deepening crisis at ARM, Morgan Stanley actively worked with and counseled ARM as to ways ARM could

attempt to improve its situation. This advice from Morgan Stanley to ARM included advice on how to maximize ARM's benefit to the detriment of Morgan Stanley's client, General American.

103. Although Morgan Stanley continued its attempts to prop up ARM, at the expense of General American, in the hopes of hiding Morgan Stanley's own exposure, those attempts failed.

M. THE COLLAPSE

104. On July 29, 1999, ARM announced substantial 2nd quarter losses that resulted in a downgrade of ARM's credit rating.

105. As Morgan Stanley anticipated, shortly after ARM's downgrade, General American was downgraded, which in turn triggered the put of substantially all of the short put GICs. This was the scenario Morgan Stanley foresaw almost five years earlier.

106. Because General American was unable to raise billions of dollars in cash necessary to cover its short put GIC obligations, in addition to over one billion dollars in cash needed to cover other GIC redemptions, it was forced to seek receivership protection, all to its damage as hereinafter claimed.

107. By Morgan Stanley's own calculations, General American was valued at two-billion, two-hundred and fifteen million dollars (\$2,215,000,000.00), as of December 11, 1998.

108. Morgan Stanley was paid over six million dollars to value General American during the forced sale stemming from the run on the bank.

109. On August 25, 1999, Morgan Stanley, by its own calculations in a fairness opinion signed by Derek Kirkland, valued General American at one-billion, two-hundred million dollars (\$1,200,000,000.00).

110. Accordingly, by Morgan Stanley's own calculations, General American was

damaged by over one billion dollars in just nine months.

N. MORGAN STANLEY'S MOTIVES

111. As ARM's majority owner and as lead underwriter for each of ARM's common offerings, as lead underwriter on ARM's preferred offering and as analyst touting the stock as a "Strong Buy," Morgan Stanley made numerous public misrepresentations and numerous failures to disclose regarding ARM's true and accurate financial condition. As a result, Morgan Stanley knew that ARM's collapse would subject Morgan Stanley to significant, and valid, claims and litigation for actual and punitive damages.

112. Additionally, Morgan Stanley was concerned that disclosure of ARM's true financial condition would result in meritorious lawsuits being filed against Morgan Stanley.

113. Considering the substantial conflict of interest resulting from the representation of two entities so closely tied by the short put GIC product and the related reinsurance agreement, Morgan Stanley should have refused to counsel, advise, aid and abet, ARM and should have promptly, fully, and fairly disclosed to General American's Board of Directors all of the problems and risks relating to ARM and the short put GICs, because Morgan Stanley already owed fiduciary duties to General American.

O. PUNITIVE DAMAGES

114. In addition to Morgan Stanley's failure to inform General American's Board of Directors of the inherent, and apparent, dangers of General American's relationship with ARM, Morgan Stanley actively advised and represented that ARM was a "Strong Buy."

115. On November 13, 1998, just one day after Moody's Investors Services changed the outlook on ARM to negative from stable, Morgan Stanley analyst Michael W. Blumstein issued a research update acknowledging Moody's Investors Services change in outlook. However, Blumstein derogated Moody's Investors Services November 12, 1998, Rating Action,

expressing Morgan Stanley's view that this change in outlook was not a "major negative."

116. Morgan Stanley, in its continued effort to "pump up" ARM so as to avoid the liability Morgan Stanley expected would arise from ARM's collapse, emphasized that Moody's did not formally "downgrade" ARM. In this update, Morgan Stanley also expressed its belief that ARM's GICs were "[w]ell structured and underwritten and that the mortgage-backed securities are appropriate for the company's floating rate contracts."

117. Morgan Stanley expressly maintained its "Strong Buy" in further analyst statements in 1999, all the while knowing of ARM's problems, and knowing of the blatant inaccuracies expressed in Morgan Stanley's update. These "Strong buy" recommendations continued in 1999 despite, and contrary to, Morgan Stanley's more honest assessment of ARM and the short put GICs as expressed to ARM, including at the January 1999, and February 1999, presentations to ARM's Board of Directors.

118. Morgan Stanley's use of its analysts in misrepresenting the status of companies with which it has a relationship is not limited to ARM, but has instead been continuous and repeated. Morgan Stanley has been fined and or reprimanded by regulatory authorities, including New York's Attorney General Elliot Spitzer, for similar conduct involving conflicts of interest relating to Morgan Stanley's research analysts and Morgan Stanley's investment banking activities. In total, those fines have amounted to well over one hundred million dollars.

119. As further indication that Morgan Stanley's acts were designed to further its own financial self-interest, reflecting an evil motive and reckless indifference to General American, Morgan Stanley put back (*i.e.* redeemed) its own 30-day put GIC on March 1, 1999. That action, when considered in context with ARM's imminent collapse and the detrimental impact this would have upon General American, shows even further Morgan Stanley's overriding self-

interest. Morgan Stanley put its GIC put just four days before General American was downgraded. Morgan Stanley knew of the imminent downgrade and executed its GIC in order to protect its own financial interests. Again, Morgan Stanley conducted this action without notifying General American's Board of Directors of the problems Morgan Stanley knew would ultimately result in harm to General American.

120. Further, Morgan Stanley assisted ARM in obtaining excessive fees from General American as part of the recapture of ARM's trust assets backing its GIC obligations.

121. Moreover, even as ARM was collapsing, Morgan Stanley encouraged General American to purchase ARM. Morgan Stanley proposed this transaction so as to further disguise Morgan Stanley's own malfeasance in relation to ARM's offerings.

P. BACKGROUND OF RUBENSTEIN

122. Leonard Rubenstein started with General American as a junior securities analyst in 1972.

123. Like most insurance companies, General American invested the insurance premiums it received as one avenue of achieving profits. To that end, General American purchased controlling interest in Conning to serve as General American's investment manager. While Conning was an independent corporation, it served as General American's major asset manager. Rubenstein ultimately became President and Chief Executive officer of Conning. General American compensated Conning, and specifically Rubenstein, based upon the total assets under management that Conning retained for General American. Thus, as the size of the General American portfolio grew so did Rubenstein's compensation.

124. As CEO of Conning, Rubenstein's primary responsibility was to oversee the investment of capital which General American received from its insurance and investment activities, including the proceeds of General American's GIC sales. As part of those duties,

Rubenstein was charged with reporting directly to the Investment and Risk Committee of General American's Board of Directors.

125. General American's Investment and Risk Committee was formed to review and consider investment related risks contained within General American's portfolio. In his reports to that committee, Rubenstein negligently omitted pertinent information in relation to the short put GIC product.

126. As an officer of General American, Rubenstein owed a fiduciary duty to General American to advise General American's Board of Directors of the risks associated with the GICs and of ARM's precarious financial condition.

127. If General American were to have reduced or eliminated its short put GIC holdings, Rubenstein's compensation would have been substantially reduced.

V. CAUSES OF ACTION

COUNT I

Fraud Against Morgan Stanley

128. Paragraphs 1 through 127 are incorporated herein by reference.

129. As set forth previously herein, Morgan Stanley made specific, false, material representations and statements to General American's Board of Directors.

130. Morgan Stanley knew that the representations made to General American's Board of Directors were false.

131. General American's Board of Directors did not know of the falsity of Morgan Stanley's representations.

132. General American's Board of Directors rightfully relied on the truth of Morgan Stanley's representations.

133. Morgan Stanley wanted and intended for General American's Board of Directors to rely upon the truth of Morgan Stanley's representations.

134. As a direct result of Morgan Stanley's representations, General American was damaged by over one billion dollars as calculated by Morgan Stanley's own valuation.

135. In making these representations to General American's Board of Directors, Morgan Stanley acted out of its own financial self-interest and in a manner that reflects an evil motive and reckless indifference to General American's rights, justifying an award of punitive damages.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Morgan Stanley and Morgan Stanley & Co. Incorporated, jointly and severally, on Count I and thereupon award the Liquidators, in their capacity as Liquidators of General American Mutual Holding Company actual damages in an amount in an amount that is fair and reasonable, disgorgement of Morgan Stanley's profits and fees received in connection with these matters, punitive damages at or in excess of three billion dollars (\$3,000,000,000.00), the Liquidators' costs herein incurred, and such other and further relief as the Court deems just and proper.

COUNT II
Fraudulent Omission/Fraudulent Concealment Morgan Stanley

136. Paragraphs 1 through 127 are incorporated herein by reference.

137. As set forth previously herein, Morgan Stanley concealed material facts which Morgan Stanley had a duty to disclose to General American's Board of Directors, during the time in which General American had engaged Morgan Stanley as investment banker.

138. Morgan Stanley intended that General American's Board of Directors would rely on Morgan Stanley's duty to fully disclose all relevant facts, analyses and information.

139. By virtue of its superior knowledge, and by virtue of its fiduciary relationship with General American, Morgan Stanley had a duty to disclose these facts to General American's Board of Directors.

140. General American's Board of Directors did not know of Morgan Stanley's material omissions.

141. General American's Board of Directors rightfully relied on Morgan Stanley's duty to disclose as General American's Board of Directors had hired Morgan Stanley to advise it on exactly the representations in question.

142. As a direct result of Morgan Stanley's fraudulent omissions, General American was damaged by over one billion dollars as calculated by Morgan Stanley's own valuation.

143. In concealing these facts from General American's Board of Directors, Morgan Stanley acted out of its own financial self-interest and in a manner that reflects an evil motive and reckless indifference to General American's rights, justifying an award of punitive damages.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Morgan Stanley and Morgan Stanley & Co. Incorporated, jointly and severally, on Count II and thereupon award the Liquidators, in their capacity as Liquidators of General American Mutual Holding Company actual damages in an amount in an amount that is fair and reasonable, disgorgement of Morgan Stanley's profits and fees received in connection with these matters, punitive damages at or in excess of three billion dollars (\$3,000,000,000.00), the Liquidators' costs herein incurred, and such other and further relief as the Court deems just and proper.

COUNT III
Breach of Fiduciary Duty Against Morgan Stanley

144. Paragraphs 1 through 127 are incorporated herein by reference.

145. As set forth previously herein, a fiduciary duty existed between General American and Morgan Stanley as a result of Morgan Stanley's engagement as General American's Investment Banker in relation to the proposed demutualization of General American Mutual Holding Company.

146. As General American's Investment Banker, Morgan Stanley agreed to provide unbiased advice, information, and guidance relating to General American's financial situation and proposed demutualization.

147. As Investment Banker Morgan Stanley assumed the responsibility of becoming intimately familiar with General American's financial conditions in order to provide competent, unbiased, advice to General American's Board of Directors.

148. As Investment Banker, Morgan Stanley assumed a duty of loyalty to General American.

149. Through this relationship Morgan Stanley developed a fiduciary relationship, and duty, to General American.

150. Morgan Stanley breached its fiduciary duty to General American as alleged herein, including by inappropriately advising General American's Board of Directors to continue the sale of General American GICs, and by failing to advise General American's Board of Directors of the risks associated with the GICs and ARM's precarious financial condition.

151. As a direct result of Morgan Stanley's breach of its fiduciary duty to General American, General American was damaged by over one billion dollars.

152. In breaching its fiduciary duty to General American, Morgan Stanley acted out of its own financial self-interest and in a manner that reflects an evil motive and reckless indifference to General American's rights, justifying an award of punitive damages.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Morgan Stanley and Morgan Stanley & Co. Incorporated, jointly and severally, on Count III and thereupon award the Liquidators, in their capacity as Liquidators of General American Mutual Holding Company actual damages in an amount that is fair and reasonable, disgorgement of Morgan Stanley's profits and fees received in connection with these matters, punitive damages at or in excess of three billion dollars (\$3,000,000,000.00), the Liquidators' costs herein incurred, and such other and further relief as the Court deems just and proper.

COUNT IV
Negligent Misrepresentation Against Morgan Stanley

153. Paragraphs 1 through 127 are incorporated herein by reference.

154. As set forth previously herein, Morgan Stanley made numerous, specific misrepresentations and statements to General American's Board of Directors, during the course of Morgan Stanley's engagement as General American's investment banker.

155. Morgan Stanley intentionally provided the information for the guidance of General American's Board of Directors.

156. General American's Board of Directors justifiably relied on the information Morgan Stanley provided.

157. As a direct result of Morgan Stanley's misrepresentations, General American was damaged by over one billion dollars as calculated by Morgan Stanley's own valuation.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Morgan Stanley and Morgan Stanley & Co. Incorporated, jointly and severally, on Count IV and thereupon award the Liquidators, in their capacity Liquidators of General American Mutual Holding Company actual damages in an amount that is fair and reasonable,

disgorgement of Morgan Stanley's profits and fees received in connection with these matters, the Liquidators' costs herein incurred, and such other and further relief as the Court deems just and proper.

COUNT V
Negligent Misrepresentation Against Rubenstein

158. Paragraphs 1 through 127 are incorporated herein by reference.

159. As set forth previously herein, Leonard Rubenstein made misrepresentations to General American's Board of Directors, and specifically to the Investment and Risk Committee of General American's Board of Directors. These misrepresentations occurred during the course of Rubenstein's tenure as Chairman and CEO of Conning.

160. The misrepresentations made by Rubenstein were false due to Rubenstein's failure to exercise reasonable care.

161. General American justifiably relied on the information provided by Rubenstein.

162. As a direct result of General American's reliance on Rubenstein's misrepresentations, General American was damaged.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Leonard Rubenstein on Count V and thereupon award the Liquidators, in their capacity as Liquidators of General American Mutual Holding Company actual damages in an amount that is fair and reasonable and further award the Liquidators their costs, expenses, and such other and further relief as the Court deems just and proper.

COUNT VI
Breach of Fiduciary Duty Against Rubenstein

163. Paragraphs 1 through 127 are incorporated herein by reference.

164. As set forth previously herein, Rubenstein owed General American a fiduciary duty as a result of Rubenstein's position as an Officer of General American.

165. As an Officer of General American and CEO of Conning, Rubenstein was required to provide analysis, information, and guidance relating to General American's investment portfolio.

166. As CEO of Conning, Rubenstein assumed the responsibility of becoming intimately familiar with General American's investment portfolio in order to provide competent, unbiased, advice to General American's Board of Directors.

167. Rubenstein had a fiduciary relationship with, and owed fiduciary duties to General American.

168. Rubenstein breached his fiduciary duty to General American as alleged herein, by inappropriately advising General American's Board of Directors to continue the sale of General American GICs, and by failing to advise General American's Board of Directors of the risks associated with the GICs.

169. As a direct result of Rubenstein's breach of his fiduciary duty General American was damaged.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Leonard Rubenstein, on Count VI and thereupon award the Liquidators, in their capacity as Liquidators of General American Mutual Holding Company actual damages in an amount in an amount that is fair and reasonable, the Liquidators' costs herein incurred, and such other and further relief as the Court deems just and proper.

COUNT VII
Professional Negligence Against Morgan Stanley

170. Paragraphs 1 through 127 are incorporated herein by reference.

171. Morgan Stanley owed General American a duty of care as General American's Investment Banker. Morgan Stanley failed to meet its duty of care by failing to use the degree of

care commensurate with the skill and proficiency commonly exercised by ordinarily skillful, careful and prudent investment banking professionals, and by failing to provide the degree of loyalty owed by careful and prudent investment banking professionals to their clients.

172. As set forth previously herein, Morgan Stanley not only failed to meet even what would be considered minimum requirements for an investment banker, but also affirmatively acted so as to harm the interests of its client, General American.

173. As an investment banker, Morgan Stanley had a legal duty to conform to a certain standard of conduct to protect General American from the risks it sought to avoid in seeking the investment banking relationship.

174. Morgan Stanley breached its duty owed to General American by not only neglecting to provide General American's Board of Directors with accurate information, but also by affirmatively misrepresenting General American's actual position and risks so as to further Morgan Stanley's efforts to hide its scheme to avoid liability for ARM's collapse.

175. As a direct result of Morgan Stanley's acts and omissions, General American was damaged by one billion dollars as calculated by Morgan Stanley's own valuation.

WHEREFORE, the Liquidators respectfully pray that this Court enter judgment in their favor and against Morgan Stanley and Morgan Stanley & Co. Incorporated, jointly and severally, on Count VII and thereupon award the Liquidators, in their capacity as Liquidators of General American Mutual Holding Company actual damages in an amount that is fair and reasonable, disgorgement of Morgan Stanley's profits and fees received in connection with these matters, the Liquidators' costs herein incurred, and such other and further relief as the Court deems just and proper.

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